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No. 135

In the Supreme Court of the United States

OCTOBER TERM, 1960

AVERY BRUNDAGE AND ELIZABETH D. BRUNDAGE,
PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

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OPINIONS BELOW

The findings of fact and conclusions of law of the district court (R. 83–88) are not officially reported. The opinion of the court of appeals (Pet. A4–A16) is reported at 275 F. 2d 424.

JURISDICTION

The judgment of the court of appeals was entered on February 5, 1960 (Pet. A17). Timely petitions for rehearing and for rehearing *en banc* were denied on March 30, 1960 (Pet. A18–A19). The petition for a writ of certiorari was filed on June 9, 1960. The

jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTIONS PRESENTED

Under a plan of liquidation of a parent corporation, its stockholders were entitled to receive, upon presentation of their stock certificates, a specified number of shares of the common stock of a subsidiary. The questions presented are:

1. Whether dividends becoming payable on the subsidiary's stock after the effective date of the plan were taxable to holders of the parent's stock who had not yet exercised their unconditional right to receive the stock of the subsidiary.

2. Whether, if not, that part of the proceeds of a sale of the parent's stock after the effective date of the plan which was allocable to the right to receive the dividends then payable on the subsidiary's stock was taxable as ordinary income.

3. Whether dividends declared on the subsidiary's stock by a resolution passed before the effective date of the plan but payable only if and when the plan was consummated were taxable to the parent corporation or to the persons entitled to receive the subsidiary's stock upon consummation.

STATUTES AND REGULATIONS INVOLVED

The relevant statutes and regulations are set forth in the petition at pp. A1–A3.

STATEMENT

1. On October 11, 1947, the United States District Court for the District of Oregon confirmed a plan of reorganization of the Portland Electric Power Co. ("Portland") (R. 24–44). The plan, effective February 2, 1948, provided for Portland's dissolution and the distribution to its securityholders of all its assets, consisting principally of the common stock of its subsidiary, Portland General Electric Co. ("PGE") (R. 10–24). The common stock of PGE was to be reclassified for the purpose, and holders of the prior preference stock of Portland were to receive, for each share, $6\frac{1}{2}$ shares of the reclassified PGE stock (R. 16–17, 19). On or before the effective date of the plan, the reclassified stock of PGE was delivered to an exchange agent for distribution to the participants under the plan upon surrender of their Portland securities (R. 6). The decree of confirmation declared all Portland securities to be "null and void" except for purposes of the transfer and exchange provided for by the plan (R. 42), and all rights to participate under the plan were to lapse upon a failure of any securityholder to present his bond or stock certificate within ten years of the final decree (R. 6–7; 22).

2. Prior to the effective date of the plan but in anticipation of its consummation, the board of directors of PGE adopted resolutions declaring dividends to be paid on its reclassified stock upon consummation of the plan. The resolution of July 7, 1947, after reciting that the plan contemplated PGE's issuance

of reclassified stock and the distribution of that stock to the Portland securityholders, declared a dividend of $3 a share on the reclassified stock "to be paid to the holders of said reclassified common stock * * * when and if the same is reclassified and issued pursuant to" the plan "after * * * consummation of said plan of reorganization shall have been completed," the resolution to be null and void if the plan were not consummated (R. 44–46). Substantially similar resolutions, each declaring a $0.45 dividend, were adopted on November 12 and December 22, 1947 (R. 47–50).

After the effective date of the reorganization plan, on March 10 and June 8, 1948, PGE declared two more $0.45 dividends, the resolutions providing that if there were Portland securityholders who had not yet exchanged their Portland securities for PGE stock "then this dividend shall be paid to said holders if and when [PGE stock] is issued to such holders [pursuant to the reorganization plan]. It is intended that this dividend shall be paid at the time of the issuance of [PGE stock] in accordance with said plan of exchange and pursuant to an assignment of dividends from the Independent Trustees of Portland * * * to said stockholders of [PGE] who have not prior to the record date * * * made the exchange of" Portland securities for PGE stock (R. 50–53).

The confirmation decree of October 11, 1947, acknowledged the $3 dividend declared by PGE on July 7, 1947, and directed PGE, upon the plan's becoming effective, to segregate the dividend in a special ac-

count and thereafter distribute it "to the persons entitled to receive [the PGE stock] under said plan of reorganization." Any dividends subsequently declared were to be similarly segregated and paid "to the holders of its reclassified stock upon the issuance of such stock to the persons entitled thereto under the said plan" (R. 41–42). The several dividends were in fact paid over to the exchange agent for disbursement to the participants under the plan upon the exchange of their Portland securities for the PGE stock (R. 6).

3. Petitioners, as of the effective date of the plan, owned 3,633 shares of the prior preference stock of Portland and, as noted above, were entitled under the plan to receive 6⅓ shares of PGE stock for each such share. They did not, however, exercise their right to surrender their Portland stock for the PGE stock but rather sold the Portland stock itself to third parties at various times during 1948 (R. 4–5, 7). The total dividends which had become payable on the PGE stock allocable to petitioners' Portland stock before the dates on which they sold their Portland stock amounted to $103,091.25 (R. 88).

On their income tax return for 1948, petitioners reported their entire gain on the sales of their Portland stock ($468,032.16) as a long-term capital gain (R. 4). The Commissioner held that $103,091.25 of the proceeds of the sales represented the dividends accrued on the PGE stock and was taxable as ordinary income (R. 8–9). The resulting deficiency was paid and in due course this suit for refund was brought

(R. 9). The district court upheld the Commissioner's determination (R. 83–88), and the court of appeals affirmed (Pet. A4–A16).

ARGUMENT

1. When the reorganization plan became effective on February 2, 1948, petitioners became unconditionally entitled to receive the PG&E shares allocable to their Portland stock, together with any dividends becoming payable on the stock. The stock and dividends were delivered to the exchange agent, there simply to await petitioners' demand for them. Both the stock and the dividends were thus unqualifiedly subject to petitioners' demand and hence constructively received by them. It follows that petitioners were taxable on the dividends on the PG&E stock when they first became payable (Regs. 111, § 29.42-2 and 3; *Corliss* v. *Bowers*, 281 U.S. 376).

Petitioners' contention that they had only an unexercised "option" to acquire the PG&E stock in an "exchange" for their Portland stock is misleading to the extent that it implies that their right to the PG&E stock was conditioned upon their giving up a separate property interest of value. After the effective date of the plan, Portland stock was "null and void" for any purpose other than to entitle the holder to the PG&E stock. It thus ceased to be "stock" at all and became neither more nor less than a certificate evidencing that right. To obtain the PG&E stock, petitioners had but to exercise their right to demand it.

giving nothing in exchange. Their "option", if it be called that, was simply an "option" either to assert their unconditional rights or to allow them to lapse by time.

2. While we think it clear that the dividends were constructively received by petitioners when they first became payable to the exchange agent, it makes no difference in this case (since all the events occurred in a single taxable year) if the transaction is viewed instead as an anticipatory assignment of income which petitioners later sold their rights to the PGE stock and the accrued dividends thereon. Petitioners had a vested right, by merely surrendering their Portland stock certificates to the transfer agent, to receive the dividends already paid on the PGE stock. They could not convert that accrued right to ordinary income into capital asset by selling it, and the portion of the purchase price attributable to the dividends already declared and payable was taxable as ordinary income. Cf. *Commissioner v. P. G. Lake, Inc.*, 356 U.S. 260; *Hort v. Commissioner*, 313 U.S. 28; *Helvering v. Horst*, 311 U.S. 112.

3. Petitioners contend alternatively that, even if they had received the PGE stock on the date the plan became effective, the previously-declared dividends

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For that reason, *Pacific Co. v. Commissioner*, 70 F. 2d 1 (C.A. 9), alleged by petitioners to be in conflict, is not in point. There the parent corporation continued to exist and to pay dividends on its own behalf, its stockholders simply being given the option to give up a continuing stock interest in the parent in exchange for a direct stock interest in the subsidiary. Patently no taxable event occurred until the option was exercised.

then payable should be treated as having been paid in the first instance to *Portland* (and presumably taxable to it) and then distributed to petitioners, not as "dividends" from PGE, but as a liquidating distribution from Portland.[7] The fallacy in the argument is that the dividends, although declared by resolutions adopted before the effective date of the plan, were expressly made contingent upon consummation of the plan and hence were payable only after the rights to the PGE stock had become vested in the Portland securityholders to whom it was to be distributed. Petitioners became entitled to the dividends on the PGE stock not by a distribution of miscellaneous cash from Portland but solely by virtue of their rights to the PGE stock given them by the plan before the dividends became payable, and Portland itself never acquired any beneficial interest in the dividends.

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[7] The same contention is also made as to the dividends declared after the effective date of the plan, but the taxability of those dividends is *a fortiori* to the taxability of the previously-declared dividends.

[8] In *Kirby* v. *Commissioner*, 35 B.T.A. 578, reversed on other issues, 102 F. 2d 115 (C.A. 5), relied on by petitioners (Pet. 14), the very premise of the decision was a finding that the stock in the hands of the liquidating trustees on which the dividends were paid had not, when the dividends were paid, been "set apart for him [the stockholder of the liquidating corporation to whom the funds were ultimately paid over] without substantial limitation or restriction as to time or manner of payment or use or enjoyment by him" but were rather still in the control of the trustees and, indeed, subject to various suits and injunctions preventing their distribution (35 B.T.A. at 599). Here, to the contrary, when the dividends became payable (upon consummation) the PGE stock was unqualifiedly available to petitioners on demand.

CONCLUSION

The decision below is clearly correct and there is no conflict. The petition for a writ of certiorari should be denied.

Respectfully submitted.

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JULY 1960.